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THE WALL STREET JOURNAL.

Power and Peril: America's Supremacy and Its Limits; Trade-Off: As China Surges, It Also Proves A Buttress to American Strength; Beijing Feeds a Giant Appetite In U.S. for Low-Cost Goods And Borrowed Capital; The Wood-Furniture Paradox

Andrew Higgins. **Wall Street Journal.** (Eastern edition). New York, N.Y.: Jan 30, 2004. pg. A.1

Subjects: Series & special reports, Trade relations, International trade

Classification Codes 9190, 9179, 1300

Locations: United States, US, China

Author(s): Andrew Higgins

Article types: News

Publication title: Wall Street Journal. (Eastern edition). New York, N.Y.: Jan 30, 2004. pg. A.1

Source Type: Newspaper

ISSN/ISBN: 00999660

ProQuest document ID: 534621591

Text Word Count 1896

Article URL: http://gateway.proquest.com/openurl?url_ver=Z39.88-2004&res_dat=xri:pqd&rft_val_fmt=info:ofi/fmt:kev:mtx:journal&genre=article&rft_dat=xri:pqd:did=000000534621591&svc_dat=xri:pqil:fmt=text&req_dat=xri:pqil:pq_clntid=11969

Abstract (Article Summary)

One of Logitech's big sellers is a wireless mouse called Wanda, which sells to American consumers for around \$40. Of this, Logitech takes about \$8, while distributors and retailers take \$15. A further \$14 goes to suppliers that provide Wanda's parts: A Motorola Inc. plant in Malaysia makes the mouse's chips, and America's Agilent Technologies Inc. supplies the optical sensor. Even the solder comes from a U.S. company, Cookson Electronics, which has a factory in China's Yunnan province next to Vietnam.

China's pivotal role in the global supply chain buttresses a pillar of foreign policy dating all the way back to 1899, when the U.S. pushed for an Open Door Policy making China's ports available to all. In turn, China's trade opening to the world in the past two decades softened its once-antagonistic foreign policy. Last year, as the U.S. prepared to invade Iraq, Beijing stood aloof from the Paris-Berlin- Moscow axis of outspoken opposition. It has offered the U.S. some help trying to curb North Korea's nuclear ambitions.

The U.S. has been a net capital importer since at least the 1980s. This is in stark contrast to Britain at the height of its imperium before World War I, when the British had net foreign assets valued at 150% of their own GDP. America, though often described as Britain's successor as the world's dominant power, does the opposite. Recent figures from the Commerce Department's Bureau of Economic Analysis show that foreign holdings of U.S. stocks, bonds and other assets exceeded America's foreign assets to the tune of \$2.3 trillion -- or 22% of GDP -- at the end of 2002.

Full Text (1896 words)

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[Second in a Series]

DONGGUAN, China -- Frank Lin joined fellow Chinese furniture makers at a hotel here last summer to discuss some alarming news from America: U.S. furniture companies were asking Washington to investigate "illegal" Chinese trade practices and restrict Chinese sales to the U.S. Among the petitioners was one of Mr. Lin's longtime customers, Virginia-based Hooker Furniture Corp.

Mr. Lin's dismay turned to confusion days later when he received an e-mail from Hooker's chief executive. Hooker looked forward to an "exciting future" doing business with China, said the message, and wanted to "continue the extraordinary growth we have had in the last few years with Asian imports."

Indeed, thanks largely to the imports, Hooker has boomed. It closed a factory in North Carolina last summer but has boosted profits and dazzled investors with a stock that more than quadrupled in two years.

"I just don't understand what they are doing. It makes no sense," Mr. Lin said after receiving the e-mail in August. On his desk lay designs sent from America. Lining the wall, newly crafted chairs stood ready for inspection by U.S. buyers. "If they don't import, they die. They need us. So why do they want to hurt us?" Mr. Lin wondered.

His bewilderment flows from a much bigger tension besetting U.S. economic relations with China -- and the economic forces that underpin America's global hegemony. China's rise both supports the American superpower and embodies some of its self-generated vulnerabilities.

Burgeoning business ties with China have become treacherous terrain. Anxious to calm workers' worries about jobs, and fearful of appearing unpatriotic, even some U.S. companies that rely on China are joining industry coalitions clamoring to curb the "China threat."

But there's another side to China's dynamism. China is slotting itself into the global economic order that America dominates and largely created. As a critical link in this capitalist chain, nominally communist China helps enrich companies such as Hooker. At the same time, it supports a central feature of America's superpower status: its gargantuan appetite for foreign goods and capital.

Though America is sometimes loosely called an empire, it defies the imperial economic script described by Lenin (who called imperialism "the highest form of capitalism"). The U.S. doesn't seek vassal states as outlets for surplus capital. In an anomaly for such a powerful nation, America sucks in money from abroad. With its large national debt and trade deficits, the U.S. binds not by lending but by borrowing and by importing.

Its status as a "hyper-debtor" makes this "hyper-power" oddly reliant on weaker partners, says Niall Ferguson, a professor at New York University and scholar of imperial history. "If you are dependent on the willingness of others to hold your assets, there is a limit to how unilaterally you can act."

For all their nation's power, many Americans feel an economic insecurity, for which China is a lightning rod. Its blitzkrieg thrust into U.S. markets over the past decade, many worry, reveals a soft economic core under the tough carapace of America's military might. From bed frames to circuit boards, the industrial bedrock of American power is crumbling, say some politicians and pundits. At stake, warns the American Furniture Manufacturers Committee for Legal Trade, which filed the complaint that upset Mr. Lin, "is our way of life, our culture and the competitiveness of America in the world."

China's emergence as a major economic power is beyond doubt. Its \$1.2 trillion economy, while far smaller than the \$10.4 trillion economy of America and Japan's \$4 trillion output, is on track to catch up with Japan inside of two decades. Already, China's growing economic weight, including a voracious consumption of crude oil, is giving Beijing commensurate influence in geopolitics -- another power center for America to contend with.

Also undeniable is a painful loss of U.S. manufacturing jobs to a country where the average plant worker earns around \$80 a month, less than an American on minimum wage makes in two days. Cheap labor pushed China's trade surplus with the U.S. to \$123 billion in a recent 12-month period, five times the gap a decade ago.

The figures, however, mask the many ways in which the world's two biggest continental economies complement each other. China's rests heavily on industry, with manufacturing, mining and related activities accounting for 51% of gross domestic product, by World Bank figures. America generates only a quarter of its GDP from industry and just 14% from manufacturing. Services contribute nearly three quarters.

Curbing Chinese imports through tariffs or a stronger yuan would only drive up imports from other countries, contends Stephen Roach, chief economist at Morgan Stanley. The only real alternative, he says, is for Americans to spend less and save more: "When Americans get frustrated with China, they should look in the mirror."

They could also look inside things they buy from China. Take the 20 million "made in China" computer mice shipped to the U.S. each year by Logitech International SA, a Swiss-American company with headquarters in California. The mice are put together in a six-floor building in Suzhou, a Chinese city once famous for its Confucian gardens but now better known as a frenetic manufacturing hub.

Logitech's Suzhou parts warehouse is a microcosm of the global economy, and helps explain why China reinforces America's role as ringmaster. Piled to the ceiling on blue metal shelves are boxes marked with the logos of foreign companies, from big U.S. multinationals to a small Belgian billiard company that makes trackballs.

One of Logitech's big sellers is a wireless mouse called Wanda, which sells to American consumers for around \$40. Of this, Logitech takes about \$8, while distributors and retailers take \$15. A further \$14 goes to suppliers that provide Wanda's parts: A Motorola Inc. plant in Malaysia makes the mouse's chips, and America's Agilent Technologies Inc. supplies the optical sensor. Even the solder comes from a U.S. company, Cookson Electronics, which has a factory in China's Yunnan province next to Vietnam.

Marketing is led from Fremont, Calif., where a staff of 450 earns far more than 4,000 Chinese employed in Suzhou. China's take from each mouse comes to a meager \$3, which covers wages, power, transport and other overhead costs.

Other Chinese-made products rely less on U.S. components and use Japanese, Korean or Taiwanese parts instead. But, in many cases, the upshot for China is the same: Foreigners get the bulk of the money. They supply many of the parts, often own the plants in China that assemble them, and get a markup on sales abroad. Foreign companies account for more than three-quarters of China's high-tech exports. The Chinese Ministry of Commerce's ranking of "China's" top 10 exporters includes two American companies -- Motorola and hard-drive maker Seagate Technology.

Logitech, like most tech, toy and textile companies with plants in China, employs mostly young women such as Wang Yan, an 18-year-old from the impoverished rural province of Anhui. She is paid \$75 a month to sit all day at a conveyor belt plugging three tiny bits of metal into circuit boards. She does this 2,000 times a day. To earn extra money, she gets up at 6 a.m. to tidy the dormitory space she shares with a dozen fellow workers.

This is her second stint in a factory. Before coming to Suzhou, she skipped school to become an underage worker at an electronics plant not far from Mr. Lin's furniture company in Dongguan. She complains about her salary but isn't going back to her village. That would mean only "eating bitterness," she says.

China's pivotal role in the global supply chain buttresses a pillar of foreign policy dating all the way back to 1899, when the U.S. pushed for an Open Door Policy making China's ports available to all. In turn, China's trade opening to the world in the past two decades softened its once-antagonistic foreign policy. Last year, as the U.S. prepared to invade Iraq, Beijing stood aloof from the Paris-Berlin-Moscow axis of outspoken opposition. It has offered the U.S. some help trying to curb North Korea's nuclear ambitions.

China's explosive growth as an exporter, though distressing for many American plants, prods the U.S. in a direction it has been moving for decades. Hooker furniture, which now imports more than 40% of the furniture it sells, mirrors this shift, scaling back on domestic manufacturing but expanding in services such as design, distribution and marketing. Meanwhile, other American companies, such as Intel Corp., focus on making high-end products, many of which end up in goods sold in America as "made in China."

China also does well out of an arrangement that provides millions of jobs, lets China steadily increase military spending and has created the biggest foreign-currency reserves after Japan's. Because of the U.S. debt habit, the arrangement also leaves China with leverage over America.

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figures from the Commerce Department's Bureau of Economic Analysis show that foreign holdings of U.S. stocks, bonds and other assets exceeded America's foreign assets to the tune of \$2.3 trillion -- or 22% of GDP -- at the end of 2002.

"America is certainly a hegemon and may be occupying Iraq but, economically at least, it does the opposite of what Lenin described as imperialism," says Angus Maddison, a British economist whose many books include a survey of the world economy over the last millennium.

(MORE)

China's Changing Picture

The world confronting China, 25 years ago and today

Population

Then: 975 million

Now: 1.3 billion

Leader

Then: Deng Xiaoping

Now: Hu Jintao

Number of private sedans

Then: 0

Now: 3 million

Fashion icon

Then: Jiang Qing

Now: Gong Li

Oil imports

Then: 0

Now: 2 million barrels a day

Annual U.S.-China trade

Then: \$2.3 billion

Now: \$177 billion*

Trade balance

Then: \$1.1 billion surplus for U.S.

Now: \$123 billion deficit for U.S.*

Currency

Then: Non-convertible

Now: Convertible in trade **

Stock trading

Then: None

Now: Two exchanges ***

Unresolved territorial claims

Then: Hong Kong, Macao, Taiwan, Soviet border region,

South China Sea islands

Now: Taiwan, South China Sea islands

* December 2002 through November 2003

** Beijing pegs yuan at 8.28 to a U.S. dollar

*** Shanghai and Shenzhen, listing 1,287 stocks in all

Milestones

- 1979: Deng steers post-Mao China on "capitalist road"
- 1981: China convicts "Gang of Four" radicals, including Mao's widow, Jiang Qing
- 1989: China crushes pro-democracy protest in Tiananmen Square
- 1990: Reopens Shanghai Stock Exchange, closed since '49 revolution
- 1997: Deng dies; China regains Hong Kong from British
- 1999: Regains Macao, enclave Portugal had held since 16th century
- 1999: Protests as U.S. accidentally bombs Chinese embassy in Belgrade
- 2000: Cracks down on Falun Gong quasi-religious group
- 2001: Joins World Trade Organization
- 2001: Chinese jet collides with U.S. spy plane over South China Sea, prompting diplomatic standoff
- 2002: Communist Party says it will admit capitalists
- 2003: SARS outbreak
- 2003: U.S., Japan urge China to float yuan; it declines
- 2003: Mass march for democracy in Hong Kong

Source: WSJ research

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